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SUBJECT: PRIVATIZATION AND PRICES REVIVE TURKEY'S COAL AND STEEL
REGION

1.(SBU) Summary: In a recent visit to the Black Sea coal and steel towns of Zonguldak and Ereğli, we were struck by the economic revival over the past two years. Privatization of state coal and steel enterprises combined with strong global prices have made a noticeable difference, providing further evidence that Turkey's strong economic growth is neither a mirage nor solely benefiting elites in Turkey's major cities. End Summary.

No Sign of Steel Privatization Controversy

2.(SBU) In a visit to Ereğli and Zonguldak on Turkey's western Black Sea coast, we found a striking change from an earlier visit in 2004. We began in Ereğli, headquarters of Erdemir, until recently one of Turkey's largest state-owned enterprises. The town's economy is dominated by the giant Erdemir steel complex, the locus of a majority of Erdemir's production capacity. Erdemir had \$3.1 billion in sales in 2005 and net income of \$143.5 million. Erdemir's privatization process had stirred intense controversy, including anti-privatization lawsuits by labor unions and demonstrations in Ereğli itself. Oyak, the military pension fund conglomerate won the tender and took a controlling share in the company in February, [12006](#).

[13](#). (SBU) In Ereğli we met first with Erdemir's new management, led by Oyak EVP Aydin Muderrisoglu, a former business school professor in the U.S. Muderrisoglu and other Oyak executives were very pleased with the acquisition of Erdemir. Even though eyebrows were raised at the size of Oyak's winning \$2.77 billion bid for 46.12% of Erdemir, Oyak now feels vindicated by Erdemir's strong profitability, helped by high world steel prices and booming local demand from Turkey's automotive, white goods, and construction industries. Muderrisoglu said the Turkish market consumes 9 million tons of steel and Erdemir produces 3.9 million. He emphasized that the steel business is a global business with prices of Erdemir's principal inputs and products determined by global markets and priced in dollars. For this reason, he said the recent fall in the exchange rate and jump in interest rates will have little impact on Erdemir's profitability.

[14](#). (SBU) Oyak is continuing and expanding the \$2 billion investment program begun by the previous public sector managers. Another Oyak executive, Ergun Okur, who is overseeing Erdemir's other large complex in Iskenderun in Southeast Turkey, told us much of the investment program is focused on the Soviet-origin Iskenderun operation rather than the more modern Erdemir complex.

5.(SBU) Following our visit, Oyak announced it had appointed a career Erdemir executive, Oguz Ozgen to run the company. Ozgen, who

took us on a tour of the plant, had managed Erdemir's Romanian subsidiary.

6.(SBU) The Government's decision to privatize Erdemir had sparked protest marches in Eregli and Ankara and was publicly attacked by former Erdemir CEO Kerim Dervisoglu. Now, however, the controversy seems to have died down. Muderrisoglu told us Oyak is not feeling any local resentment. Under the terms of the privatization tender Oyak committed not to reduce staff by more than 5% during the first 3 years of their management control.

17. (SBU) At Eregli municipality, we met with Deputy Mayor Ruan Cinar and a colleague who was also a foreman at Erdemir. They had no complaints about the privatization. Erdemir employs 7,000 people in Eregli - a town of 82,000. Given Erdemir's vital importance to the town, the municipal officials said the local population's concerns were understandable but that people were reassured once Oyak won the tender. Although the steel company still dominates Eregli's economy, a new shipbuilding factory is due to open later this year using steel from Erdemir and will create 5,000 additional jobs.

Newly Prosperous Atmosphere in Coal Town

18. (SBU) Even more striking was the difference two years had wrought the coal mining town of Zonguldak. The town's main hotel had built a modern, upscale wing and the Chamber of Commerce had moved from a cramped old building to a large steel and glass edifice. When we came two years ago, Chamber of Commerce President Salih Demir told us Zonguldak was "the last Communist town in Turkey," hopelessly dominated by the leftist coal miner's union, and the perennially loss-making state-owned coal company. The data lends some support to this view of Zonguldak: the province has the least income inequality in Turkey as measured by the Gini coefficient.

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19. (SBU) The state coal company, TTK, was not even slated for privatization because it was deemed politically impossible, and the apparatchik-like manager who received us in 2004 was unwilling to disclose the company's (embarrassingly bad) financial information to a visiting American diplomat.

110. (SBU) In 2006 we found the former TTK CEO had been replaced, and the new Deputy General Manager, Cetin Onur, was quite open with us. Though he admitted that TTK was still losing money, he explained that its management was trying to reduce the size of the loss, mostly by privatizing operation of some of TTK's mines. This strategy avoided the political controversy of privatizing TTK as a whole and had succeeded beyond management's expectations. Salih Demir, whose company operates one of the privatized mines, told us the private mines now produce 4,000 tons of coal while TTK-operated mines produce 6,000 tons. Onur told us TTK is trying to reduce costs by gradually reducing "above-ground" staff, whose numbers had grown during the bad old days of political management of TTK.

111. (SBU) Both the Chamber of Commerce President and Mayor Secaattin Gonca told us about attempts to diversify the local economy. Salih Demir described an ambitious scheme to develop a new industrial zone about 20 kilometers east of Zonguldak in the Filyos valley. The new site would be near the new Zonguldak airport, but is also expected to have a port, a power plant and, it is hoped, a new oil refinery and other factories. Shortly after we visited Zonguldak, Turkish newspapers reported that Russia's Lukoil was planning to build a new refinery near Zonguldak, one of several new refinery projects under consideration in Turkey. The location would allow Black Sea tankers to unload crude to be refined for the Turkish market without the tankers having to pass through the congested Bosphorus straits.

12.(SBU) Both in Eregli and Zonguldak, government officials and business people were hopeful that they could develop more of a tourist industry in the region given the proximity of the region's beaches to Istanbul and Ankara. The area boasts dramatic green hills rising from the Black Sea coast. In Zonguldak, however, the

Mayor and the TTK executives admitted they desperately needed funding for a new sewage and wastewater system, given that wastewater currently flows untreated into the Black Sea.

Comment:

¶13. (SBU) Zonguldak and Ereğli may not be the most representative regions from which to draw conclusions about the broader Turkish economy, since high world prices for steel and coal have had such a big impact on the two major local industries. However, the visibly improved atmosphere can also be attributed to good economic policy at the national level. From the broadest perspective, the macroeconomic policies spurred strong growth in many industrial sectors that has translated into strong demand for coal and steel. More specifically, the GOT's push to reduce the role of the public sector in the economy through privatization was key. Even before Erdemir was privatized, the Government had put in place steel company management who were trying to run the company along private sector lines, and Oyak's takeover is expected to continue to make Erdemir a more efficient, globally competitive producer.

¶14. (SBU) In the case of TTK, the success of its privatization of individual mines has reduced TTK's losses and created employment in the privately-operated mines. With so many ordinary Turks asserting that the strong growth data exaggerate Turkey's economic success, the turnaround in Ereğli and Zonguldak casts doubt on the frequently-heard thesis that the growth is only benefiting elites in Turkey's large cities.
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